Financial

Due Diligence Report

prepared by

Taylor Torrington and Associates

for

[redacted] **("Acquirer")**

in respect of

[redacted] **("Target")**

as at

[redacted] **2019**

Introduction

1. Background

1.1. Taylor Torrington and Associates has been requested by [redacted] herein after referred to as (the "**Acquirer**") to undertake a financial due diligence investigation (the "**Investigation**") of the business and affairs of [redacted] ("[redacted] or the "**Target**").

1.2. The principal aim of the Investigation is to identify any potential or contingent financial risk associated with the Target which may have an impact on the negotiation, structuring and implementation of the proposed acquisition of 100% of the [redacted]est in the Target by the Acquirer (the "**Proposed Transaction**").

1.3. The scope of the Investigation is limited to the information made available to Taylor Torrington and Associates for the purpose of disclosing confidential information to the Acquirers and their advisors.

2. Format of this due diligence report ("Report")

This document is divided into three sections:

2.1. this introductory section, including the status of this report, Taylor Torrington and Associate's assumptions in preparing this Report, and definitions;

2.2. the red flag issues report, with key issues and suggestions going forward relevant to the Proposed Transaction; and

2.3. the key issues list, being an executive summary of the material issues described in the Report.

3. Status of this report

3.1. This Report sets out the results of the Investigation and the review performed by Taylor Torrington and Associates in relation to the various documents furnished to and reviewed by Taylor Torrington and Associates.

3.2. This Report sets out only those findings which in the professional discretion and opinion of Taylor Torrington and Associates are material issues which have a bearing on either the implementation of the Proposed Transaction or which would have a material influence on the Acquirers' decision whether or not to proceed with the implementation of the Proposed Transaction. In the circumstances, the potential for undisclosed documents, arrangements, agreements and financial information which may constitute a risk for the Acquirers in relation to the Proposed Transaction does exist.

3.3. This Report pertains only to the financial aspects of the documentation provided to us and we have not specifically reviewed or commented on any legal, scientific or technical aspects in this Report.

3.4. As such, Taylor Torrington and Associates sought to isolate, through the Investigation and based on the documentation provided, those material issues relating to the Target of which the Acquirers should be aware in order to determine whether the Proposed Transaction should occur.

3.5. This Report is to be considered as part of the overall process of due diligence being undertaken by and on behalf of the Acquirers in relation to the Target and the Proposed Transaction and is not to be taken in isolation. We do not accept responsibility for assessing the technical implications of the documents or information reviewed by us (as such a review would require, among other things technical and industry knowledge and expertise as well as a full understanding of the Acquirers' strategic plans), although we have sought, where possible, to highlight matters which we consider, in our professional discretion and opinion, to be commercially significant. Accordingly, this review should not be seen as a substitute for examination of appropriate documents and materials by technical personnel and advisors.

3.6. This Report does not contain a detailed description of each document reviewed and its purpose is to set out those material financial issues which we consider, in our professional discretion and opinion, to be material in the context of the Proposed Transaction. Reliance should not be placed solely on any of the summaries contained in this Report, which are not intended to be exhaustive of the provisions of any document or circumstances. It is important to note that the Investigation does not consist of a full and comprehensive due diligence investigation.

3.7. Unless otherwise expressly agreed by us in writing, no person other than the Acquirers is entitled to rely on this Report, and we shall have no responsibility or liability to any party who has access to this Report, whether in contract, delict (including negligence) or otherwise.

3.8. It is recorded that this Report is strictly confidential and may not be released to any person who has not signed the appropriate release letter in favour of Taylor Torrington and Associates.

4. Scope of the Investigation

4.1. The Target was furnished with a due diligence data questionnaire setting out those documents and information which Taylor Torrington and Associates required for consideration in the Investigation.

4.2. Documentation was made available via Microsoft OneDrive and email.

4.3. In accordance with our instructions, any legal and technical issues were specifically excluded from the scope of our review in this Report.

5. Assumptions

This Report has been prepared on the basis of the following assumptions:

5.1. any scanned or photocopied documentation made available to us are complete and true copies of the originals, any accounting system information exports have not been amended in any way, power and authority (to the extent that any of the documentation and/or information made available to us turns out to be inaccurate, incorrect or false, we make no representation as to the accuracy and completeness of this Report);

5.2. the information reflected in the documents provided is accurate – we have not verified such accuracy independently;

5.3. there have been no variations to the documentation as presented to us;

5.4. the terms of such documentation have been complied with in all respects;

5.5. the reports and opinions expressed are not adversely affected by the laws of any jurisdiction other than those of South Africa;

5.6. the documents and information provided by the Target are all that is necessary in order to address the issues under Investigation or all that is in fact available; and

5.7. except where expressly stated by us to the contrary all transfer duties and/or similar duties, taxes or levies relating to the documents and the transactions contemplated therein have been paid in full on the due date.

6. Disclaimer

6.1. This Report is addressed to the Acquirer solely for their use and benefit and may not be transmitted to any other person without our prior written consent, except in those instances where the Acquirers may be obliged by law to do so.

6.2. This Report may not be relied upon by any person other than the Acquirers and may not be used for any purpose other than the consideration by the Acquirers of the Proposed Transaction. We shall accordingly not accept any responsibility for any loss or damage suffered by any person other than the Acquirers as a result of reliance on the contents of this Report.

6.3. We reserve the right to amend this Report in the light of any new information received but do not undertake any obligation to do so.

7. General Definitions

The following definitions should be used to the extent relevant:

7.1. "**Acquirer**" means [redacted];

7.2. "**CIPC**" means Companies and Intellectual Property Commission;

7.3. "**Companies Act**" means the Companies Act 71 of 2008;

7.4. "**Distribution Agreement**" means the agreement entered into between [redacted] Target and [redacted] [redacted] (therein referred to as the Supplier) for the supply and distribution the [redacted] product;

7.5. "**Insurance Policy**" means the insurance policy entered into between [redacted] and the Target in respect of the business of the Target;

7.6. “**Premises**” means the leased premises situated at [redacted];

7.7. “**Proposed Transaction**” the transaction whereby 100% of the [redacted] in the Target will be purchased by the Acquirer from the Seller;

7.8. “**SARS**” means the South African Revenue Service;

7.9. “**Seller**” means [redacted];

7.10. “**Supplier**” means [redacted] (owner of the [redacted] product name);

7.11. “**Target**” means [redacted] [redacted] (Registration: [redacted]);

7.12. “**VAT**” means value-added tax in terms of the Value-Added Tax Act 89 of 1991;

Red Flag Issues Report

Summary of key findings and suggested actions going forward

1. **Inventory**

The Acquirer indicated that not all stock items have been booked into the system, nor has a proper stock count been performed. The Acquirer should perform a stock count and identify slow moving or obsolete inventory. A detailed inventory list reconciled to the Management Accounts should be provided.

2. **Cash and cash equivalents**

Cash and cash equivalents as per the [redacted] Management Accounts were R[redacted], [redacted].

The Acquirer must confirm that [redacted] has full rights and legal entitlement to all money that is disclosed. [redacted].

3. **Disclosures in the Financial Statements and to SARS relating to Income Tax and VAT**

The Financial Information submitted to SARS on the ITR14 for [redacted] and in the VAT201 Returns for [redacted] and [redacted] did not match the Financial Information reflected in the Financial Statements.

If revenue and profits disclosed to SARS have been understated, then there are material Income Tax penalties and interest that could be due, which would necessitate a large adjustment to the Financial Statements to record the new liability, with a consequential decrease in NAV in the Target, as well as serious cash flow implications.

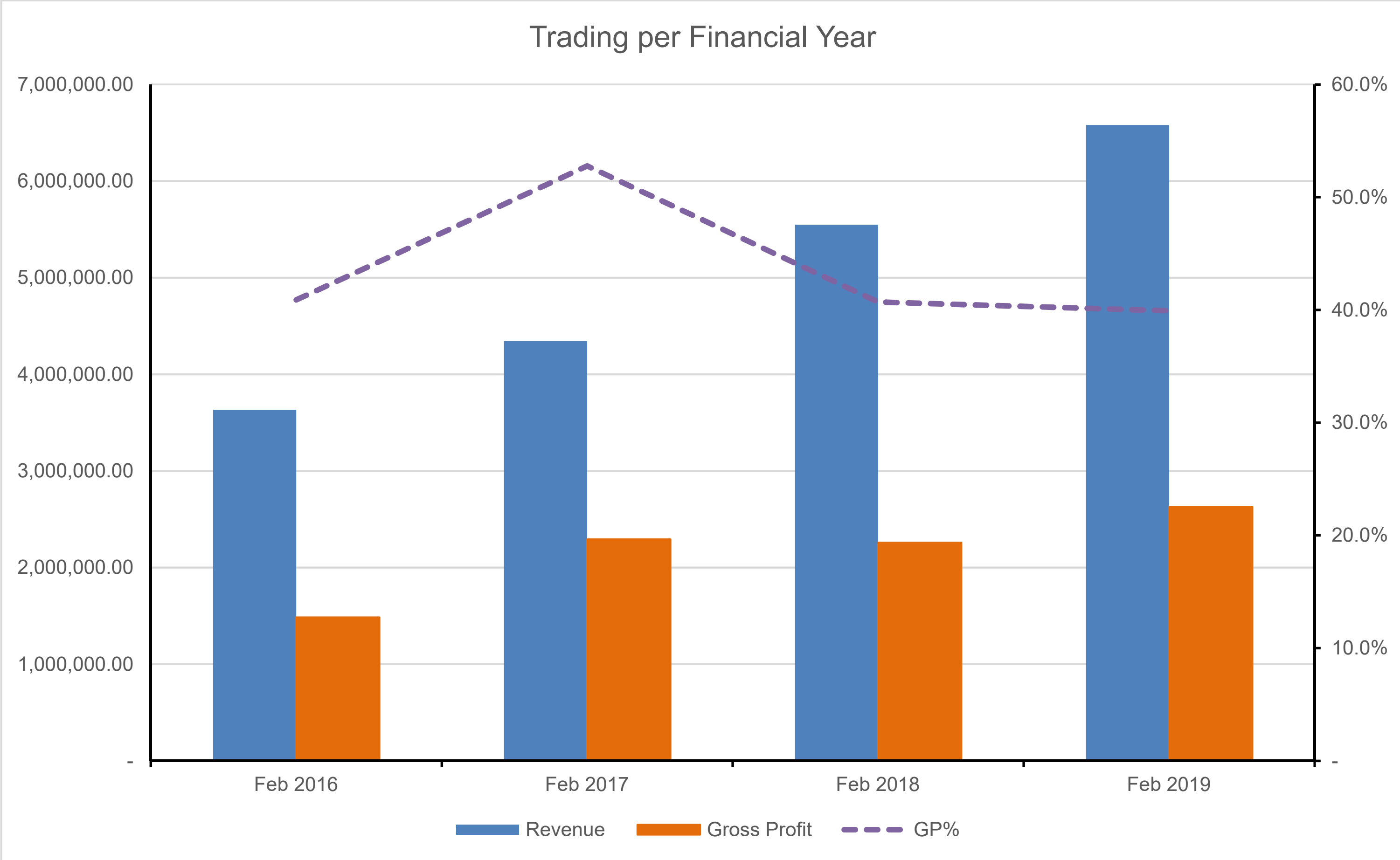
If revenue and profits disclosed in the Financial Statements have been overstated, then the Financials should be restated and audited, potentially with new accountants and auditors. This will materially affect the enterprise value of the Target.

If the revenue and profits in the Financial Statements are a true reflection of trading performance, and there has been material understatement of tax payments and liabilities, then the nature of the Proposed Transaction should be altered to rather purchase the business of the Target out of the actual legal entity and start operating out of a new legal entity, as opposed to acquiring the Members Interest in the CC.

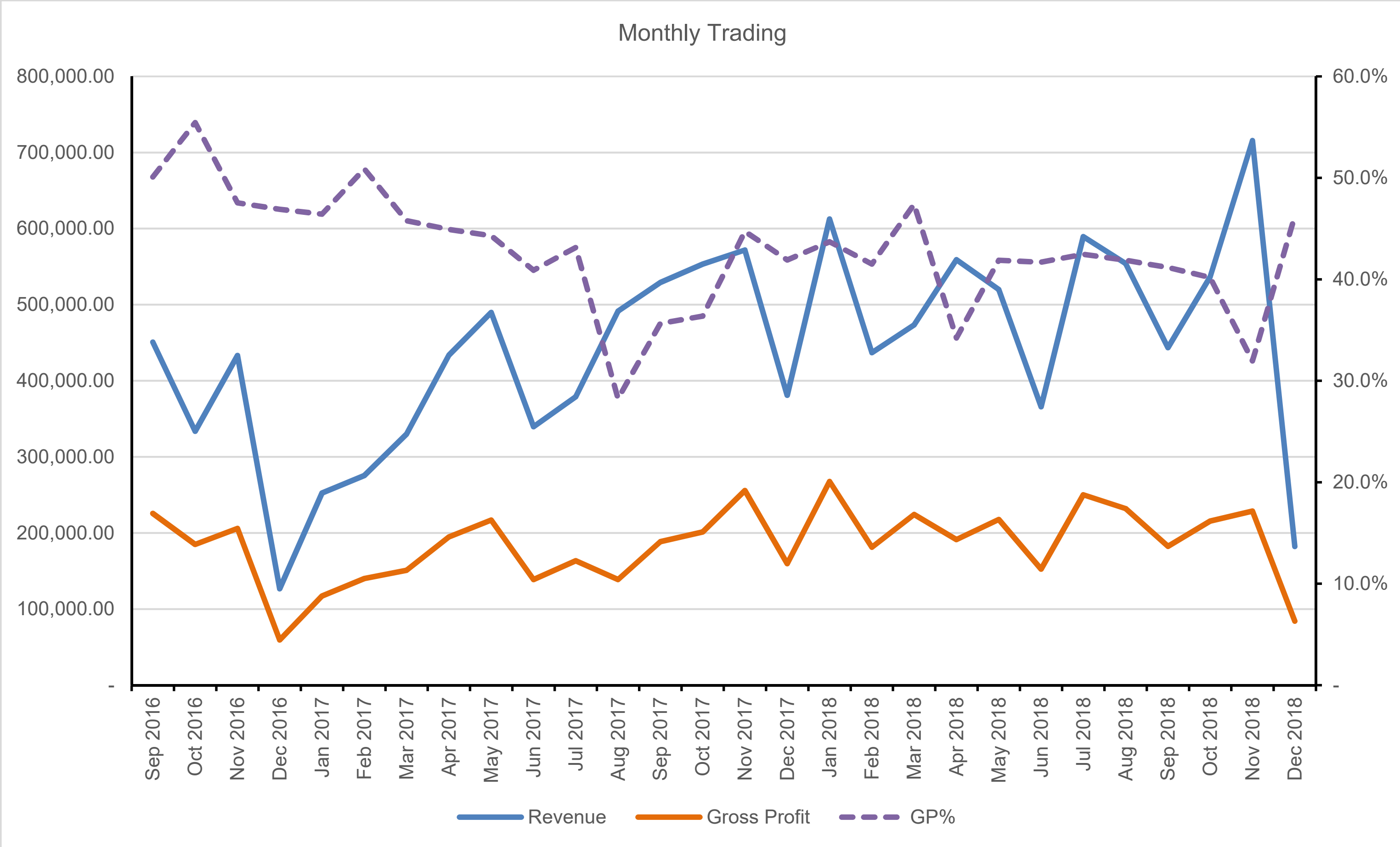
4. Employees Tax

All people doing work for the Target are treated as independent contractors. However, they all need to be properly evaluated in terms of their status as employees vs independent contractors to avoid being possibly deemed as employees, resulting in potential Employees tax penalties and interest.

Key issues/ information		Implication and/or possible mitigation
1.	**Trading** The Financial Statements and Management Accounts show robust and consistent revenue growth over the past 3 Financial Years: [redacted] equating to a cumulative average growth rate of [redacted]% in total revenue growth over this time. Gross Profit margins have remained high at approximately [redacted]%. It was noted that there was a spike in GP Margin in [redacted] to [redacted]%, which might warrant further investigation. Revenue appears to be high enough (with current GP margins) to provide sufficient headroom above breakeven point to cover overheads. The headroom over the past 3 Financial Years has been: [redacted]. As an example, in [redacted], the overheads were [redacted]. At a GP margin of [redacted]% the breakeven revenue would be [redacted], cost of sales would be [redacted], and gross profit would be [redacted]. Thus the actual revenue of [redacted] was [redacted]% more than the breakeven revenue amount of [redacted].	***Implications*** The trading strength of the target appear to be strong based on the data received. However, there are some discrepancies that have been identified further on in this document that must be addressed. ***Mitigation*** Further investigation in the underlying data might be necessary. The Acquirer should consider including additional profit warranties by the Seller in the Proposed Transaction, or possibly adjusting the purchase price to allow for any risk of misstatements in the trading history that has been presented.



Trading per Financial Year
7,000,000.00
6,000,000.00
5,000,000.00
4,000,000.00
3,000,000.00
2,000,000.00
1,000,000.00
-
60.0%
50.0%
40.0%
30.0%
20.0%
10.0%
-
Feb 2016
Feb 2017
Feb 2018
Feb 2019
Revenue
Gross Profit
GP%


Monthly Trading
800,000.00
700,000.00
600,000.00
500,000.00
400,000.00
300,000.00
200,000.00
100,000.00
-
60.0%
50.0%
40.0%
30.0%
20.0%
10.0%
-
Sep 2016
Oct 2016
Nov 2016
Dec 2016
Jan 2017
Feb 2017
Mar 2017
Apr 2017
May 2017
Jun 2017
Jul 2017
Aug 2017
Sep 2017
Oct 2017
Nov 2017
Dec 2017
Jan 2018
Feb 2018
Mar 2018
Apr 2018
May 2018
Jun 2018
Jul 2018
Aug 2018
Sep 2018
Oct 2018
Nov 2018
Dec 2018
Revenue
Gross Profit
GP%

2.	**Financial Statements** Financials Statements have been provided for [redacted] Feb 2019 Financials Statements are not yet complete. The Acquirer has indicated that he has had sight of signed cover sheets (signed by the Director and the Preparer), however, these have not been provided for the purpose of this Due Diligence report. The Financial Statements are not required to be audited as the Public Interest score is below [redacted] However, very low financial reliance can be placed on unaudited financials.	***Implications*** There could be possible misstatements in the Financial Statements as audits have not been conducted. ***Mitigation*** The Acquirer should consider including additional profit warranties by the Seller in the Proposed Transaction, or possibly adjusting the purchase price to allow for any risk of misstatements in the trading history that has been presented.
3.	**Plant and equipment** A list has been provided illustrating a book value of total plant and equipment of R[redacted], but the list does not have itemized values. It is also not clear if the Acquirer has physically verified the existence and condition of all the items on the list.	***Implications*** Items might not actually exist at the premises. Items might not all be legally owned by the Target. Items might need repairs or maintenance if their condition has not been verified. The market value of items might differ materially from the book value. ***Mitigation*** The Acquirer should physically verify the existence and condition of all the items on the list. The Acquirer should also consider the actual market value of

		items, and possibly conduct some independent price checks on significant items as a reasonability test.
4.	**Vehicles** There are [redacted] vehicles with a combined Book value of R[redacted]. Individual values have not been provided. A reasonability test with independent price checks showed that the market value for similar makes and models of vehicles on Autotrader are approximately R[redacted] per vehicle, thus a combined market value of R[redacted] in total. Consequently, there doesn't appear to be a negative equity value in the vehicles. The Acquirer has physically verified the vehicles and confirmed their current state and condition, which appears to be adequate. The service history of the vehicles has not been verified, nor whether they are still covered by a manufacturer warranty, service plan, or motor plan. Motor vehicle ownership documents were not provided to verify the actual title holder of each the vehicles.	***Implications*** Expensive repairs and maintenance of the vehicles could be imminent should the service history of the vehicles be incomplete or questionable, or if there is no cover by a manufacturer warranty, service plan, or motor plan. Vehicles might not actually belong to the Target. ***Mitigation*** The Acquirer should consider using a qualified mechanic to technically inspect the vehicles for any adverse mechanical conditions. The Acquirer should have sight of the Vehicle Licensing Department RC1 or NCO documents to confirm actual ownership.

Vehicles Description	VW Polo	Nissan NP200	Nissan NP200	Total
Registration	[redacted]	[redacted]	[redacted]	
Mileage	[redacted]	[redacted]	[redacted]	
Year	2016	2015	2015	
Banking Institution	Standard Bank	Nissan Finance	Nissan Finance	
Original Loan value	100,130.00	134,763.96	101,135.00	336,028.96
Current Loan Value	58,169.54	45,378.22	28,704.39	132,252.15
Monthly Payment	2,323.03	2,557.43	2,277.03	7,157.49
Total Payments	61	60	60	
Payments Remaininig	26	20	13	
Settlement Date	31/05/2021	01/09/2020	02/02/2020	
Applicable Interest Rate	11.75%	11.47%	11.30%	

5. **Inventory**

A list of inventory product types was provided, along with a detailed system generated list of inventory products. However, this list was exported on [redacted] and did not have a total to agree back to the Management Accounts for [redacted]. In addition, it did not have aging categories, so it was not possible to identify slow moving stock.

The Acquirer also indicated that not all stock items have been booked into the system, nor has a proper stock count been performed.

Implications

The inventory quantity and pricing reported in the Financial Statements might be incorrect. Slow moving or obsolete inventory might be unable to be sold.

Mitigation

The Acquirer should perform a stock count and identify slow moving or obsolete inventory. A detailed inventory list reconciled to the Management Accounts should be provided.

6.	**Debtors** A detailed customer list was provided as at [redacted], as well as a customer transactions report for the month of Jan 2019, and a debtors age analysis as at [redacted]. The debtors age analysis as at [redacted] showed a balance of R[redacted], and did not reconcile back to the Management Accounts as at [redacted], which showed a balance of R[redacted]. However, the aging did show that only R[redacted] [redacted]%) of the R[redacted] was in [redacted] days and older, which is highly favourable.	***Implications*** It is vital to understand the age of debtor amounts, to identify slow paying customers, or bad debts that need to be written-off. It also has an impact on cash flow projections, and the strategy of which customers to focus on, and which ones to avoid. It appears that the proportion of long outstanding debts is very small. ***Mitigation*** The Acquirer should confirm that the debtors age analysis exported as at [redacted] reconciles to the Management Accounts as at [redacted] to ensure the Management Accounts reflect the correct balance.
7.	**Creditors** A creditors age analysis as at [redacted] that reconciles back to the Management Accounts was not available. The Acquirer has indicated that the policy of the Target is to settle all creditors within 30 days, however, this hasn't been substantiated with evidence.	***Implications*** If the system generated creditors report does not match the balance as per the Management Accounts, the possibility of unrecorded liabilities can exist. ***Mitigation*** The Acquirer should obtain the creditors age analysis that reconciles to the Management Accounts as at [redacted] to ensure the Management Accounts reflect the correct balance. The age analysis should be inspected to see if

		there are any long outstanding amounts indicating potential disputes with suppliers or possible cash flow concerns.
8.	**Cash and cash equivalents** Cash and cash equivalents as per the [redacted] Management Accounts were R[redacted], which do not agree to the Bank Statement amount of R[redacted] [redacted]). The difference is R[redacted] A further bank statement was provided ([redacted] which showed a balance of R[redacted]. However, this account is held by a different legal entity: [redacted] After adding the 2 bank accounts, there is a shortfall remaining of [redacted]. This must be explained.	***Implications*** Cash and cash equivalents appear to be materially overstated in the Management Accounts. There is also a risk that transactions going through multiple bank accounts of different entities might not be correctly recorded in the books of the Target. ***Mitigation*** The Acquirer must confirm that [redacted] has full rights and legal entitlement to all money that is disclosed. The second bank account appears to belong to an entity owned by the [redacted]. [redacted], should be listed as a Related Party, and all transactions and balances should be appropriately disclosed, possibly as a Loan Receivable, not Cash and cash equivalents.
9.	**Related parties** All legal entities and other related parties to [redacted] were required to be disclosed for the purposes of the Due Diligence. This includes subsidiaries	***Implications*** Transactions between related parties are required to be disclosed in the Financial Statements in order to comply with IFRS for SMEs. The risks

	or other companies owned by members or their families that interact with [redacted]. [redacted] appears to be a Related Party that has not previously been disclosed.	concerning related party transaction and balances are that they might not be conducted at arms length, and the true economic value of might not be accurately reflected. ***Mitigation*** All Related Parties must be properly disclosed, and all such transactions and balances must be reported.
10.	**Income Tax** The following documents were provided: 1. Tax Clearance Certificate encompassing: 1.1. Income Tax [redacted] 1.2. VAT [redacted] 2. Income tax return ITR14 for [redacted] Although the current Tax Clearance Certificate showed that the company was in Good Standing with SARS as at [redacted] the Financial Information submitted to SARS on the ITR14 for [redacted] did not match the Financial Information reflected in the Financial Statements.	***Implications*** Either: 1. The revenue and profits disclosed to SARS have been understated 2. The revenue and profits disclosed in the Financial Statements have been overstated ***Mitigation*** The Acquirer should urgently investigate this matter further with the Purchaser. The following further documents should be obtained:

		1. Income tax return ITR14 for [redacted] 2. Income tax assessment ITA34 for [redacted] 3. Provisional tax return IRP6 for [redacted] 4. Income tax Statement of Account ITSA from [redacted] 5. Tax calculations for the previous 3 years 6. List of actual payments made to SARS over the past 3 years If revenue and profits disclosed to SARS have been understated, then there are material Income Tax penalties and interest that could be due, which would necessitate a large adjustment to the Financial Statements to record the new liability, with a consequential decrease in NAV in the Target, as well as serious cash flow implications. If revenue and profits disclosed in the Financial Statements have been overstated, then the Financials should be restated and audited, potentially with new accountants and auditors. This will materially affect the enterprise value of the Target. If the revenue and profits in the Financial Statements are a true reflection of trading performance, and there has been material understatement of tax payments and liabilities, then the nature of the Proposed Transaction should be altered to rather purchase the business of the Target out of the actual legal

		entity and start operating out of a new legal entity, as opposed to acquiring the Members Interest in the [redacted].

Statement of Comprehensive Income

	Financials	Income Tax ITR14	Variance	[redacted]
	[redacted]	[redacted]	[redacted]	
Revenue	[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]	[redacted]

11.	**VAT** Value added tax returns “VAT201” for [redacted] and [redacted] were inspected, with a significant variance in figures between what has been reported internally vs what has been disclosed to SARS. The VAT Statement of Account “VATSOA” from 1[redacted] to [redacted] [redacted] was provided (covering 24 trading months over 12 bi-monthly returns. A reasonability calculation showed that management accounts were showing [redacted]% higher revenue than what was reported to SARS.	***Implications*** Either: 1. The revenue and profits disclosed to SARS have been understated 2. The revenue and profits disclosed in the Financial Statements have been overstated ***Mitigation*** The Acquirer should urgently investigate this matter further with the Purchaser. The following further documents should be obtained: 3. All Value added tax returns “VAT201” from [redacted] 4. All VAT reconciliations from [redacted] If revenue and profits disclosed to SARS have been understated, then there are material VAT penalties and interest that would be due, which would necessitate a large adjustment to the Financial Statements to record this new liability, with a consequential decrease in NAV in the Target, as well as serious cash flow implications. If revenue and profits disclosed in the Financial Statements have been overstated, then the Financials should be restated and audited, potentially

		with new accountants and auditors. This will materially affect the enterprise value of the Target If the revenue and profits in the Financial Statements are a true reflection of trading performance, and there has been material understatement of tax payments and liabilities, then the nature of the Proposed Transaction should be altered to rather purchase the business of the Target out of the actual legal entity and start operating out of a new legal entity, as opposed to acquiring the [redacted] in the [redacted].

Bi-monthly VAT returns	[redacted]	[redacted]
Revenue as per management accounts	[redacted]	[redacted]
Standard rated supply of goods and services	[redacted]	[redacted]
Variance amount	[redacted]	[redacted]
Variance %	[redacted]	[redacted]

Management Accounts recalculation

VAT Period	Receipts	Payments	Net Amount	Output VAT	Input VAT	Net VAT Payment
[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Total	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]

VAT Returns

VAT Period	Receipts	Payments	Net Amount	Output VAT	Input VAT	Net VAT Payment
Mar 2017	306,126.83	(275,466.04)	30,660.79	37,594.52	(33,829.16)	3,765.36
[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]

Variance amount	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Variance %	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]

12.	**Employee expenses** It was explained that all staff are considered by the Target to be independent contractors, and none are salaried employees. Accordingly, the Target does not appear to be registered for any Payroll taxes, and Employee Tax Returns "EMP201" for PAYE, SDL, and UIF, or Employee Tax Statement of Accounts "EMPSA" from [redacted] to 28 [redacted] were not available.	***Implications*** The evaluation of the status of employees vs independent contractors is covered in great detail in Interpretation Note 17 (Issue 5) of the Income Tax Act 58 of 1962 issued on 5 March 2019. The tax implications for independent contractors are as follows: 1. Where the taxpayer is 4th schedule independent and common law independent - the taxpayer is a true independent contractor and no employee's tax is to be deducted. 2. Where the taxpayer is common law independent but does not pass the statutory exclusion (4th schedule) - Employee's tax is to be deducted on a monthly basis as follows: 2.1. If the independent contractor works more then 22 hours a week, he/she must be taxed in terms of the income tax tables. 2.2. If the independent contractor works less then 22 hours a week, he/she is to be taxed at a flat rate of 25%. Here income is to be indicated under the code 3616. This would then enable the taxpayer to claim allowable expenses against the income earned.

		2.3. If the taxpayer is a VAT vendor and provided a tax invoice, the 25% PAYE is to be deducted on the value of the invoice (therefore excluding VAT) 3. 3. Where the taxpayer is 4th schedule not independent in terms of the 4th schedule and also not independent at common law, the taxpayer is classified as an employee and subject to employee's tax like any other employee. Thus there could be a potential unrecorded Employees tax liability in the Target, which may include penalties and interest. ***Mitigation*** All people doing work for the Target need to be properly evaluated in terms of their status as employees vs independent contractors.